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Testimony

on Reauthorization of the U.S. Grain Standards Act

Before the

Committee on Agriculture, Nutrition and Forestry

U.S. Senate

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on Behalf of

National Grain and Feed Association

and North American Export Grain Association

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Chairman Chambliss and members of the Committee, I am Jerry Gibson, Regional Manager for Bunge North America Inc., in Destrehan, Louisiana. My responsibilities include management of Bunge's export elevator in Destrehan.

My testimony today is presented on behalf of the National Grain and Feed Association (NGFA) and the North American Export Grain Association (NAEGA). I serve as a member of NGFA's Grain Grades and Weights Committee and NAEGA's Grades and Inspections Committee, both of which address issues concerning the official grain inspection and weighing system and the U.S. Grain Standards Act that are the subject of this hearing.

The NGFA, established in 1896, consists of approximately 900 grain, feed, processing, exporting and other grain-related companies that operate about 5,000 facilities that handle more than 70 percent of all U.S. grains and oilseeds. The NGFA's membership encompasses all sectors of the industry, including country, terminal and export elevators; feed manufacturers; cash grain and feed merchants; end users of grain and grain products, including processors, flour millers, and livestock and poultry integrators; commodity futures brokers and commission merchants; and allied industries. The NGFA also consists of 35 affiliated state and regional grain and feed associations, as well as two international affiliated associations. The NGFA has strategic alliances with the Pet Food Institute and the Grain Elevator and Processing Society, and has a joint operating and services agreement with NAEGA.

NAEGA, established in 1912, is a not-for-profit trade association comprised of private and publicly owned companies and farmer-owned cooperatives involved in and providing services to the bulk grain and oilseed exporting industry. NAEGA member companies ship practically all of the bulk grains and oilseeds exported each year from the United States. The Association's mission is to promote and sustain the development of commercial export of grain and oilseed trade from the United States. NAEGA acts to accomplish this mission from offices in Washington D.C., and in markets throughout the world.

I also am an alternate member of the U.S. Department of Agriculture's Grain Advisory Committee, which was established under the U.S. Grain Standards Act. This committee advises the Grain Inspection, Packers and Stockyards Administration concerning its implementation of the Act and variety of program and operational issues associated with the official grain inspection system, including the agency's strategic plan, performance measures and financial management of the official grain inspection system.

At the outset, the NGFA and NAEGA strongly support reauthorization of the U.S. Grain Standards Act to preserve the official grain inspection system. Both of our organizations have a long history – in the NGFA's case, dating back to the very establishment of the Act in 1916 – in supporting a national grain inspection and weighing system. GIPSA and its designated and delegated official agencies perform a very useful and important role for the entire marketplace in maintaining the official U.S. grain standards and providing unbiased, third-party inspection and weighing of bulk grains and oilseeds at export, where the use of official services is mandatory. Further, GIPSA serves a vital role in minimizing and resolving non-tariff trade barriers that can arise in international trade. These activities enhance the efficient U.S. grain marketing system and our ability to serve global markets, and GIPSA is to be commended for its efforts. We believe a five-year reauthorization is prudent to preserve effective oversight of the agency by Congress.

But in supporting reauthorization of the U.S. Grain Standards Act, the NGFA and NAEGA urge that Congress support two critical elements that we believe are absolutely essential if the official grain inspection system is to be preserved and a federal role maintained for export grain:

- First, we urge that Congress oppose any amendment to the U.S. Grain Standards Act to authorize GIPSA to impose additional user fees to cover its grain standardization activities.

- Second, we urge Congress to amend the U.S. Grain Standards Act to give the GIPSA the flexibility to designate independent, third-party inspection agencies to perform the hands-on official inspection and weighing of grain and oilseeds at export facilities, under 100 percent GIPSA oversight using GIPSA-approved standards and procedures.

We respectfully submit that the evidence is compelling that both of these recommendations are essential to restoring the official grain inspection system's financial integrity and cost-competitiveness at export locations.

Opposition to Shifting GIPSA Standardization Activities to User Fees

First, let me address our strong opposition to amending the U.S. Grain Standards Act to authorize additional user fees to finance GIPSA's standardization activities. It's important to stress that the users of the official grain inspection system – primarily the export industry – already pay nearly 70 percent of GIPSA's grain inspection-related budget through user fees. That includes 100 percent of the direct costs of officially inspecting and weighing grain, as well as the agency's administrative, supervisory and overhead costs attributable to the performance of those duties.

What we are opposing is the imposition of **additional** user fees to cover the costs of developing, reviewing and maintaining the U.S. grain standards themselves. These activities include reviewing each of the grain standards every five years to ensure they still are meeting the needs of producers, merchants and consumers in reflecting grain quality attributes. Standardization functions also include the agency's Quality Assurance-Quality Control System, which is designed to ensure the consistent application of the grain standards nationwide to avoid inter-market grading differences. In its fiscal 2006 budget, the administration proposes to shift $4.3 million for such standardization activities to user fees.

The NGFA and NAEGA believe that the case is convincing that the U.S. grain standards benefit the entire grain marketing system – including producers and consumers of grain and grain products – because they foster accurate, consistent and efficient measurements of grain quality. Indeed, consumers are the ultimate beneficiaries of these activities because they make it possible for grain to be marketed more efficiently and at a lower cost, and result in more consistent quality characteristics in grain-based foods.

Thus, shifting GIPSA's standardization activities to user fees represents a thinly disguised **new tax** that would drive up costs and undermine the cost-competitiveness of U.S. grain and oilseed exports. That, we submit, is exactly the wrong policy prescription. Further, if the additional user fees were to be imposed on users of the official inspection in the domestic market – where use of the official services is voluntary – it would force an even greater shift to lower-cost unofficial inspection alternatives. Were the fee to be imposed on any user of the U.S. grain standards, an even broader array of U.S. agriculture would be taxed.

Every Congress since the 1980s has seen this proposal to shift grain standardization activities to user fees for what it is – an unwarranted new tax – and has rejected it. We encourage this Congress to do likewise, by **not** amending the U.S. Grain Standards Act to authorize GIPSA to impose user fees to finance its grain standardization activities.

Granting Authority for GIPSA to Utilize Independent, Third-Party Inspection Agencies to Perform Official Inspections for Export Grain

Now let me turn to our second major recommendation – one that we believe is absolutely essential if the official grain inspection and weighing system is to be cost-competitive and remain viable for bulk exports of U.S. grains and oilseeds in the future.

Specifically, the NGFA and NAEGA strongly urge Congress to amend the U.S. Grain Standards Act to authorize GIPSA to utilize independent, third-party agencies to perform the hands-on grading and weighing of grains and oilseeds at U.S. export facilities under 100 percent on-site GIPSA supervision using GIPSA-approved standards and procedures.

Let me review a few of the major elements that the NGFA and NAEGA would recommend in shifting to the use of independent, third-party agencies to perform official inspection and weighing of export grains and oilseeds:

- First, GIPSA's process for determining and approving independent, third-party agencies to perform official inspections at export should be open and transparent, done through notice-and-comment rulemaking in the ***Federal Register***.

- Second, the GIPSA-approved independent third-party agency should be responsible for hiring the inspectors. We would recommend that GIPSA license all personnel employed by such third-party agencies. Exporters should be able to contract directly with a GIPSA-approved delegated independent, third-party agency for official grain inspection and weighing services. And the fees charged should be negotiated between the exporter and the third-party agency.

- Third, and importantly, we believe that the **six state agencies that GIPSA already has delegated the responsibility for performing official grain inspection and weighing services at export ports should retain their exclusive authority. There should be no change in this feature of the official grain inspection and weighing system.**

- Fourth, as mentioned previously, GIPSA under the legislative language would retain the right to perform 100 percent on-site oversight authority at each export location to continually monitor and audit the performance of the third-party agency, and would collect a fee for performing this oversight function. GIPSA also would retain the authority to suspend or revoke the authority of the third-party agency at any time for cause.

- Fifth, GIPSA would issue final official inspection and weighing certificates based upon the results determined by the delegated third-party agency inspector operating under 100 percent GIPSA supervision. The official inspection certificate relied upon by U.S. exporters and our foreign customers would continue to be used.

- Sixth, GIPSA would maintain its comprehensive national quality-assurance and control program to ensure grading accuracy and consistency, including its appeal inspection service.

- Seventh, the proposal would be limited to commodities marketed under the U.S. Grain Standards Act – namely, corn, soybeans, wheat, sorghum, barley, canola, flaxseed, oats, rye, sunflower seed, triticale and mixed grains. Other commodities – like rice – that are marketed under the Agricultural Marketing Act would **not** be affected.

This approach is modeled after the system that has been used successfully for the past 28 years in the domestic market, where GIPSA designates official inspection authority to state and/or private agencies that operate under GIPSA review and oversight. But there are several important differences that the NGFA and NAEGA would recommend that GIPSA incorporate to provide additional safeguards that the integrity of the official inspection system will be maintained:

- First, in the case of export facilities, GIPSA should maintain 100 percent on-site supervision of the personnel hired by the GIPSA-designated independent, third-party agency to perform the actual official grading and weighing of grain. As in the case with state and private agencies that GIPSA delegates and designates to perform official inspections in the domestic market, GIPSA should set the standards for the private agency and for the performance of the inspectors. And GIPSA would retain the sole authority to suspend or revoke the license of a third-party agency at any time for cause.

- Second, GIPSA personnel should continue to test all export scales.

- Third, the proposed amendment to the U.S. Grain Standards Act would give GIPSA the authority to promulgate rules – authority we fully anticipate GIPSA would use – to require exporters wishing to utilize a GIPSA-approved independent private agency to install technology that would ensure GIPSA's ability to provide 100 percent supervision of independent third-party personnel.

- Finally, the NGFA and NAEGA would prefer that this new system be implemented as soon as possible. But in our discussions with GIPSA, it appears that it would be prudent to phase-in the new approach over a period of up to three years, beginning with lower-volume export ports where the cost of providing official inspection and weighing service is comparatively more expensive than at higher-volume export facilities. The proposed amendment provides that flexibility to GIPSA, and would allow for the program to be fine-tuned, if needed, before it is implemented at the higher-volume grain export ports. In this regard, we would recommend that report language accompanying legislation reauthorizing the U.S. Grain Standards Act include a request that GIPSA provide progress reports on implementation of independent, third-party inspection agencies as part of its already-existing annual report to Congress.

So, why make such a change?

For starters, the nature of the grain export industry and the global grain marketplace has changed dramatically in the last decade. The "old" industry model a decade ago was one where international grain traders took ownership positions in paper representing grain and sold it to a string of other traders that eventually resold the shipment as a commodity to end-users. Today, much of the international grain trade involves more direct relationships between buyer and seller. Supply chains have been established that provide for long-term stability in trading relationships and drive improvements in efficiency. These supply chains frequently are accompanied by direct foreign investment in grain-deficit countries by international grain companies to receive, process and utilize imported grains and oilseeds for grain- and animal-based food products. Thus, the "old" business model of a multi-national grain trade that provided commodities to national firms for grain processing or animal feed now is being overshadowed by international agribusiness models that increasingly are focused on grain processing and that have direct supply relationships with end-user customers.

This transformation carries huge implications, making it of paramount importance to satisfy the grain-quality attributes needed by our customers to maintain those supply relationships. If today's grain exporter does not meet the needs of its direct customer, that business is shifted to another firm more quickly, more decisively and more irrevocably than ever before.

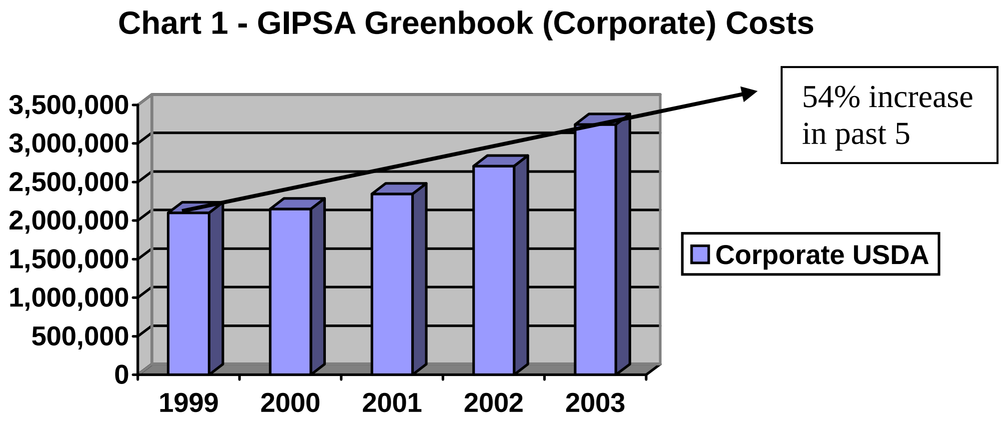
Equally important is that we're facing a far more competitive environment from very capable and efficient grain and oilseed producers and agribusinesses in foreign countries. That competition is coming from all over the world, but is most intensely felt from South America on soybeans. Since the 1996/97 marketing year, Brazil's soybean exports have increased seven-fold, the driving force behind a more than doubling of its planted acreage. Similarly, Argentina's soybean exports during the same period have increased by more than 400 percent, while its planted acres have nearly tripled. This growth also has spurred investment in both countries' transportation and grain industry infrastructure.

But South America's competitive advantage doesn't stop there. When it comes to inspection costs for grain and oilseed exports, both Brazil and Argentine farmers and exporters also have a decided cost advantage amounting to 20- to 25-cents per ton for quality inspections compared to the United States. And both countries rely upon private, third-party surveyors to perform official export inspections.

Given this intense level of competition, it is virtually impossible for U.S. exporters to shift these higher costs to foreign customers. Instead, those costs out of necessity either are absorbed by the exporter or passed back through the U.S. marketing system – eventually reaching our farmer-customers.

Confronting this global competition, U.S. exporters have responded aggressively by reducing operating costs and enhancing efficiencies wherever possible. But one operating expense remains beyond the reach of exporters' control, and has come to represent the single largest uncontrollable operating expenditure we face. And that's the cost incurred for official grain inspection and weighing services performed by GIPSA, which remains on a steadily upward spiral.

GIPSA's corporate costs – its fixed expenses for personnel and administrative overhead – have increased 54 percent in the last five years, a rate well above the underlying rate of inflation. [See Chart 1.] Under what likely represents a best-case scenario, a high-volume export elevator reports that GIPSA's inspection costs (attributable primarily to labor expense) have increased 7.2 percent per year from 2000-04, while that facility's private-sector labor costs increased by 2.5 percent annually over the same period. Further, GIPSA's fees charged to exporters for performing official inspections have increased from approximately 23 cents per metric ton in 1994 to 35 cents per metric ton on a national average under a new fee schedule implemented in 2004. And those GIPSA costs, much of which is attributable to increased labor costs, show no signs of abating.



This is not a new development. In fact, the problem has been building for some time, eating away at the competitive position of U.S. grain and oilseed exports. But the quickening pace of foreign competition and a number of other factors discussed later has provided a new sense of urgency to address this issue immediately.

What kind of costs savings could we realistically be expected to achieve?

While answering this question requires making some assumptions, since independent, third-party inspection agencies operating under GIPSA supervision do not yet exist, we believe it is realistic to believe that **immediate savings** from such a change would be about 23 percent – or $6.1 million – annually.

Here's how we arrive at that estimate. The average cost for GIPSA official inspections at export currently amounts to 35 cents per metric ton. Under the change being proposed, the agency expects that it would charge on average of 13 cents per metric ton to maintain 100 percent supervision at grain export facilities. Reputable national firms that we anticipate would bid to become private third-party agencies performing official grain inspection services at export estimate that such services could be provided within a range of 8- to 20-cents per ton, depending upon the volume of grain, the efficiency of the export elevator and other circumstances at the export port. Thus, the cost for official inspections at export would be within an estimated range of 21- to 33-cents per ton, after adding GIPSA's supervisory fee. We assume that the overall national average would be somewhat less than the midpoint of 27 cents per ton, given that the most efficient export elevators tend to operate at higher-volume ports. However, using the midpoint as a reasonable estimate average, cost savings would be expected to be about 8 cents per metric ton.

But because the cost of official inspection services in the future would be growing at a slower rate, the savings over time would expand compared to what would be expected to occur in the absence of such a change – simply because the savings would be compounded from year to year. Thus, after a decade, we estimate that the annual savings would grow to around $17.5 million, with cumulative savings of approximately $112 million over the 10-year period.

These savings are depicted graphically in Charts 2 and 3. Chart 2 shows the cost increases that could be expected to occur over the next ten years under the status quo versus under a system where independent third-parties perform official grain inspecting at export. It is based upon the continuation of the existing trend of a 7 percent annual increase in GIPSA's cost of performing official service at export facilities. That compares to a projected 2.5 percent annual increase in costs that we anticipate would occur were private agencies to perform inspections under GIPSA supervision – an assumption based upon the industry's experience with the rate of cost increases incurred from non-government private contractors providing non-inspection-related services at a major grain export facility. Chart 3 depicts what the cumulative savings would be over the next decade, based upon the "constant" of 76.2 million metric tons of export grain being officially inspected each year.

Chart 2
Estimated Annual Cost Savings
(status quo vs. delegated third-party agency)

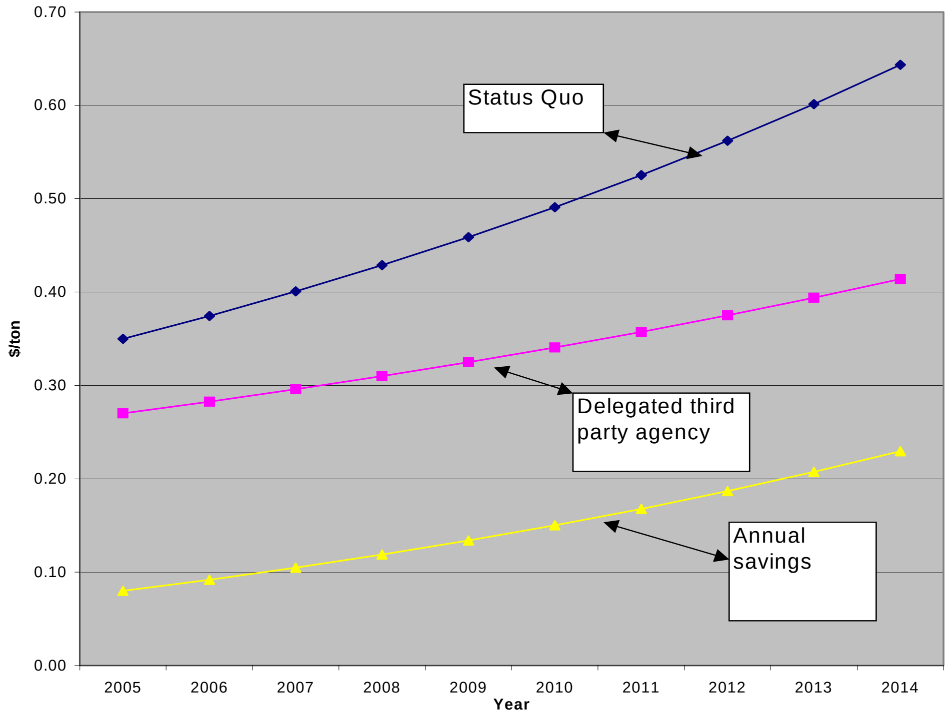
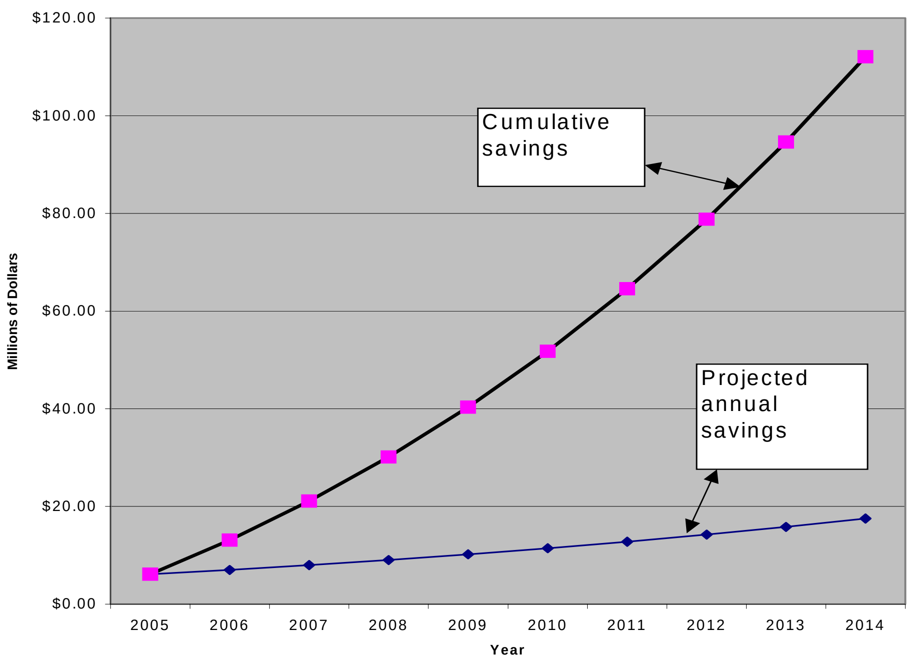
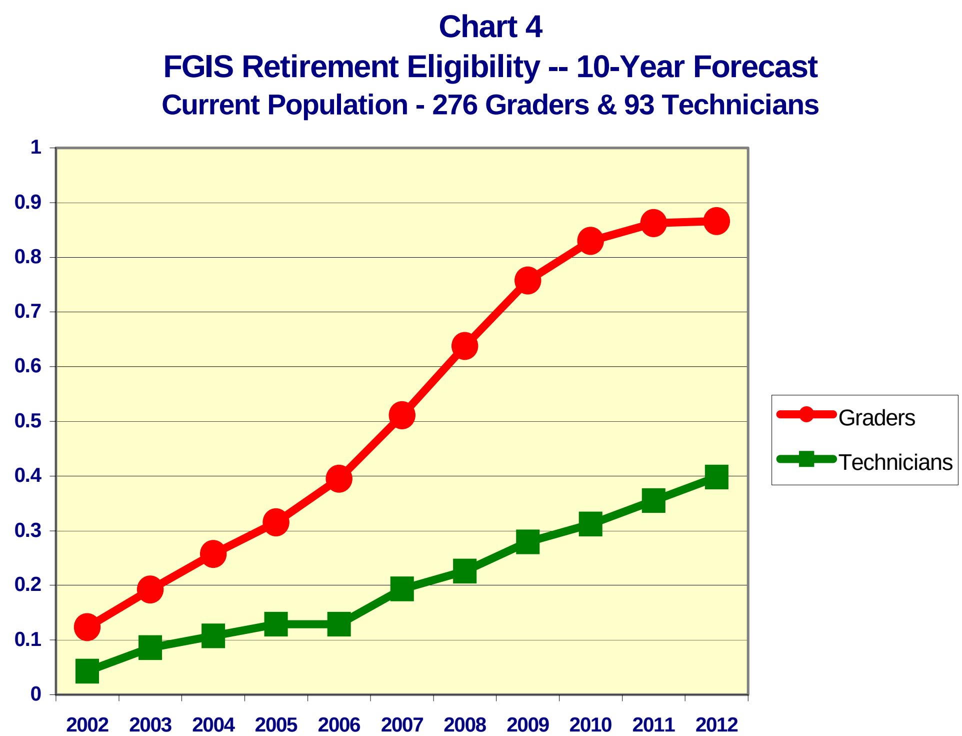


Chart 3
Estimated Cumulative Savings
(status quo versus delegated third-party agency)



Why is the time right to make such a change?

We've already discussed three of the reasons: the changed structure of the grain export industry, the fierce competitive pressures from foreign countries and the immediate and future cost savings that we believe could be achieved. But there's a fourth major reason why the time is right. And that's the aging of GIPSA's inspection work force.



As illustrated by Chart 4, 51 percent of GIPSA's 276 official grain inspectors will be eligible for retirement in 2007. Fully 70 percent will be eligible for retirement within the next five years. Making a change now would minimize the impact on federal employees, who in many cases could opt for early retirement. We actually envision that many of these inspectors would form the nucleus of a capable and highly trained inspection work force that would be available for hiring by the independent, third-party agencies that would be authorized under the proposed amendment. Further, making a change now would obviate the need for FGIS to engage in a costly and time-consuming hiring and training process to replenish its inspection work force.

So, given what we believe is the inevitability of making a change to ensure the affordability of official grain and oilseed inspections at export in the future, this clearly is an optimal time to act from a labor and human-relations standpoint.

The NGFA and NAEGA believe that this approach holds great promise for maintaining and enhancing the competitive position of U.S. grain and oilseed exports while at the same time retaining the integrity of U.S. inspection results and enhancing the long-term viability of government-based official inspection and weighing services.

We are not alone in holding this belief. Last week, six major farm and commodity organizations – the American Farm Bureau Federation, American Soybean Association, National Association of Wheat Growers, National Corn Growers Association, National Grain Sorghum Producers and U.S. Wheat Associates – joined the NGFA and NAEGA signing a letter urging Congress to adopt this approach. So did the American Association of Grain Inspection and Weighing Agencies, which represents most of the delegated private and designated state inspection agencies that currently perform official inspections for GIPSA.

Further, GIPSA's Grain Inspection Advisory Committee has weighed in on this issue, passing a resolution during its May 4-5, 2004 meeting recommending that GIPSA evaluate the benefits and methods of allowing private agencies to provide official inspection services at export grain facilities.

Conclusion

There was another time in the not-to-distant past that Congress acted to preserve the financial integrity of the official grain inspection system. During the late 1970s – a mere four years after its creation – the Federal Grain Inspection Service's administrative overhead had grown to such an extent that the ratio of administrative/supervisory personnel to actual inspectors was a staggering 2.1 to 1. For every dollar spent by FGIS to actually inspect and weigh grain, another 82 cents was being spent to "administer and supervise" the inspection and weighing system. The situation clearly was unsustainable.

As part of the budget reconciliation bill in 1981, Congress made a critically important decision. While accepting the Reagan administration's proposal to shift these FGIS administrative and supervisory costs associated with official grain inspection to the industry in the form of a user fee, Congress adopted the NGFA's recommendation to impose a hard ceiling on those costs as a percentage of the actual cost of inspecting and weighing grain. The results were dramatic. Thanks to the legislative mandate and a dedicated new FGIS administrator and his team that set about to reform the agency, FGIS's budget within three years was cut almost in half – from $62.6 million to $38 million. And its full-time work force, which had been projected to reach 2,242 in fiscal 1982, was reduced to 853 – with no noticeable impact on the quality or integrity of official inspection and weighing services.

GIPSA is to be commended for transforming itself into a much more efficient and responsive agency, with much less administrative overhead than existed previously. But today we stand at another crossroads, in which Congress has an opportunity to give this reformed and vitally important agency the authority and flexibility it needs to improve the affordability and long-term viability of official grain inspection and weighing at export facilities. The industry pledges to work with Congress and the agency to achieve this important objective.

Thank you for the opportunity to testify. I will be pleased to respond to any questions you may have.